VZCZCXRO3814
OO RUEHLMC
DE RUEHTG #0534/01 0762301
ZNY CCCCC ZZH
O 172301Z MAR 06
FM AMEMBASSY TEGUCIGALPA
TO RUEHC/SECSTATE WASHDC IMMEDIATE 1504
INFO RUEHZA/WHA CENTRAL AMERICAN COLLECTIVE PRIORITY
RUEHCV/AMEMBASSY CARACAS PRIORITY 0331
RUEHME/AMEMBASSY MEXICO PRIORITY 6227
RHEBAAA/DEPT OF ENERGY WASHDC PRIORITY
RUCPDOC/DEPT OF COMMERCE WASHDC PRIORITY
RUEAIIA/CIA WASHDC PRIORITY
RHEHNSC/NSC WASHDC PRIORITY
RUEATRS/DEPT OF TREASURY WASHDC PRIORITY
RUEHLMC/MILLENNIUM CHALLENGE CORP WASHINGTON DC PRIORITY 0372

C O N F I D E N T I A L SECTION 01 OF 02 TEGUCIGALPA 000534

SIPDIS

SIPDIS

STATE FOR EB/ESC, WHA/EPSC, WHA/PPC, AND WHA/CEN
STATE FOR S, D, E, P, AND WHA
TREASURY FOR DDOUGLASS
STATE PASS AID FOR LAC/CAM
NSC FOR DAN FISK

E.O. 12958: DECL: 03/16/2016
TAGS: EPET ENRG PGOV PREL PINR VZ HO
SUBJECT: HONDURAN FUELS: THE SEARCH FOR A CALM DIALOGUE

REF: A. (A) TEGUCIGALPA 482

¶B. (B) TEGUCIGALPA 505
¶C. (C) TEGUCIGALPA 521

Classified By: Classified By: Ambassador Charles Ford for reasons 1.4 (b) and (d).

¶1. (C) Summary: At present the decision on if and how to implement the recent decision to have the GOH itself offer a public fuel tender rests with the GOH. Over the coming weeks, however, Post plans to encourage both GOH and private sector interlocutors to engage in a process of calm and reasonable dialogue on next steps and alternatives. The sense of urgency generated by the initial burst of activity -- including the snap GOH decision to implement the import scheme (ref A), a series of Congressional and Presidential public statements on the issue (ref B), and Ambassador's private demarche on President Zelaya (ref C) -- served to generate appropriate public debate, but such overt interventions have perhaps now run their course. A public debate over the fuels issue, now in full swing (without any obvious Post involvement), has put many of the key issues on the table and seems to have slowed momentum towards precipitous GOH action. While it is far too early to definitively say that the GOH is prepared to engage meaningfully in seeking a face-saving exit from this morass, it now seems appropriate to push behind the scenes for such a dialogue. End Summary.

¶2. (C) As reported ref C, Post seeks to offer President Zelaya USG engagement on his proposal to move the country toward a liberalized fuels market. This process would be extremely delicate for the GOH both politically and economically, and would likely take three years or more to complete. Fortunately, according to former Minister of Finance William Chong Wong, a World Bank study on market liberalization already exists, paving the way to open a discussion on that topic. Moreover, according to IMF Resident Representative Hunter Monroe, the GOH's own Technical Petroleum Unit (UTP) statistics clearly indicate that in Central America liberalized markets enjoy lower fuel prices than managed ones. USG engagement on this topic would also be useful, but should, in Post's view, be confined to a limited role of impartial source of analysis and advice.

¶3. (C) According to Esso Country Manager Daniel Mencia, the oil companies themselves would welcome such a move towards liberalized markets. Mencia notes, for example, that it remains a struggle for him to persuade his corporate management to invest in Honduras because of its managed market. Liberalization would free him to compete more effectively, in his view. He lamented to Post that he had repeatedly offered to discuss such issues with the GOH, but we note that, to date, Esso has not offered a credible plan as an alternative. Esso has also offered to craft a joint public outreach campaign with the GOH to lay the foundations for such a move with the public, but this effort has been repeatedly rebuffed. Post considers that this was part of was a deliberate political strategy on the part of the GOH to set the oil companies up as the bad-guys, and notes a number of occasions on which such overtures were rejected by the GOH. The most egregious, per ex-Minister Chong Wong, was the GOH Commission of Notables refusal to take the above-cited World Bank study into account during its deliberations. According to Chong Wong, the Commission's consultant rejected the study because it did not fit his pre-conceived idea of moving to a state-managed system. (In other words, Chong alleges, the Commission picked its facts to fit the conclusion they had already decided they must reach.)

¶4. (C) That said, there are some encouraging signs that the GOH is realizing the difficult position it has placed itself in. In conversations with oil company representatives, Minister of the Presidency Yani Rosenthal has begun distancing himself from the policy, noting that he is only following the Commission's recommendations. Vice President Santos has long opposed the plan privately, and is now publicly managing-down expectations and generally showing

greater leadership in the fuels policy debate. Even President Zelaya -- a self-professed supporter of free trade -- now claims to be seeking political cover to move towards liberalized markets. While we are not convinced the will is yet there to reverse the bid solicitation process, we are hopeful there is a growing willingness to consider alternatives. As one businessman put it to Ambassador, the oil companies "need a Plan B."

¶5. (C) There is no doubt that the GOH decision to abruptly change policy regarding oil imports was ill-conceived, poorly executed, and risks alienating and discouraging both current and potential investors. On the eve of CAFTA entry into force, it was, put bluntly, a very poor policy choice. Post remains committed to using this as a teaching opportunity for the GOH, to emphasize the vital importance of transparent and participatory decision-making, and of predictable, credible rule sets in maintaining investor confidence. While the GOH actions do not imperil CAFTA, they certainly imperil its success to the extent that they cause investors to look elsewhere for their investment opportunities. Many in the business community are now making this point publicly; Post will continue to make this point in its contacts with GOH officials as well.

¶6. (C) Post has been equally frank with the oil companies themselves about the creative and constructive role they must play in resolving this situation. While Post (and to a limited extent, Washington) can provide support and perhaps leverage at key moments, the companies are responsible for engaging with the GOH in crafting a plan and selling it to the public. The GOH is in a box of its own making, but it is clearly in the oil companies' interest to help the GOH find a politically viable way out. (Comment: Nor can the companies rely on USG claims of expropriation. The current petroleum import regime is based on licenses, which Mencia admitted could be legally revoked by the GOH. Under those circumstances, it is far from clear that any expropriation has taken place, and Post feels it would be unwise for the companies to use that issue to pressurize negotiations. End

Comment.)

¶7. (C) In a March 16 meeting between Ambassador, business magnate Freddy Nasser, and EconChief, Nasser agreed with Post's analysis of both the political and economic threats posed by this situation. While Nasser could not present an exit strategy, he clearly grasped the fundamentally political nature of the problem. That said, he noted that many in the Zelaya Administration are young and inexperienced, and passionate about improving the quality of life for Honduras' poor. Educating them on the economic realities and risks posed by the GOH import plan will take time and patience. In the meantime, Nasser said he is telling his own staff to "calm down."

¶8. (C) Comment: The GOH plan, and particularly the process that led to its adoption, is dangerous for Honduras and puts at risk its future growth. The Zelaya team used a highly inflammatory social issue as political fodder, and is now paying the price. The GOH must simultaneously find a way to calm public passions on fuels while identifying a technical solution to a long-standing and complex sectoral policy problem. We don't believe the Zelaya team fully comprehends as yet how deep a hole they are in, but they are starting to. We are cautiously optimistic that, once they do, they would accept an extended hand from the oil companies and others to help them climb out. This will require creative and credible engagement by the companies, and genuine will (not political theatre) by the GOH. In the meantime, as Nasser sagely advised, both sides should take a deep breath and calm down. End Comment.

Ford
Ford